DECISION

THE COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

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DATE: JUN 18 1975

MATTER OF:

Scope of authority granted Secretary of HUD under 12 U.S.C. § 1713(k) to advance sums "pending" acquisition of multifamily projects in default.

DIGEST:

Under provisions of U.S.C. § 1713(k) Secretary of HUD may advance moneys for purpose of making necessary repairs to multifamily projects covered by mortgages which have gone into default and been assigned to him, provided that either default is cured or title to property acquired within reasonable time. After mortgage has gone into default and been assigned to Secretary of HUD, he may, in accordance with broad authority contained in 42 U.S.C. § 3535(i), restructure mortgage to defer portion of monthly principal and interest payment to end of mortgage term so as to cure default.

This decision to the Secretary of Housing and Urban Development (HUD) is in response to a letter from HUD's Office of General Counsel dated March 12, 1975, requesting a legal opinion as to whether section 207(k) of the National Housing Act, as amended, 12 U.S.C. § 1713(k) (1970) contains sufficient legal authority to permit HUD to advance moneys from its Insurance Fund for the purpose of making certain necessary repairs to multifamily projects after the insured mortgages for the projects had gone into default and subsequently been assigned to the Secretary.

The need for such authority was explained in HUD's letter as follows:

"* * * It has been our practice in dealing with the mortgagors of these multifamily projects to first attempt to work out an arrangement to bring the mortgage current. In the event that such attempts prove unsuccessful, the Secretary has then pursued a policy of foreclosing on the property or acquiring a deed in lieu of foreclosure.

"We are concerned that the effect of continuing this policy will have adverse consequences for both the low and moderate income tenants residing in the individual projects and the community at large. There is a risk that when HUD acquires title and then proceeds to resell the project, the new owners

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will no longer operate the project for low and moderate income families, but rather will increase the rental charges to effectively force the existing tenants to leave the project. Further, we believe that many nonprofit mortgagors have a deep commitment to the community in which their project is located.

"In order to assist those nonprofit mortgagors who have evidenced sound management capabilities to retain the ownership of their projects, and to insure that the projects retain their low and moderate income characteristics--policies which we feel are consistent with the policy of the National Housing Act--we are considering revising our procedures when a mortgage is assigned. More specifically, we are presently considering a proposal to be applied to subsidized multifamily projects which satisfy certain criteria whereby a portion of the monthly principal and interest payments would be deferred to the end of the mortgage terms.

"It is further believed, however, that additional funds must also be expended on these projects to provide for needed repairs and improvements. Such repairs are necessary to prevent further deterioration of the building and to insure that the project continues as a viable economic entity. We envision advancing funds to finance these improvements directly from the appropriate Insurance Fund, either the General Insurance Fund or the Special Risk Fund, depending on the section under which the project was insured. Such sums will be added to the mortgage debt. It appears that obtaining loans from the appropriate Insurance Fund is the only feasible source for obtaining money to finance these needed repairs, there being both practical and legal problems preventing loans from other sources."

The provisions of law that HUD would rely on as authority for the proposed procedure are 12 U.S.C. § 1713(k), and section 905 of the Housing and Urban Development Act of 1970, 42 U.S.C. § 3535(i). The latter code provision reads as follows:

"Except as such authority is otherwise expressly provided in any other Act administered by the Secretary, the Secretary is authorized to--* * *(5) consent to the modification with respect to the rate of interest, time of payment of any installment of principal or interest, security, or any other term of any contract or agreement to which he is a party or which has been transferred to him * * *."

We were informally advised by representatives of HUD that it is pursuant to the broad authority provided the Secretary in the last quoted provision of law that HUD proposes to restructure or recast mortgages (which upon default have been assigned to the Secretary) so that a portion of the monthly principal and interest payments would be deferred to the end of the mortgage term so as to cure the default by the mortgagor.

We would agree that under section 905 the Secretary may modify the terms of a mortgage assigned to him in the manner proposed in order to permit the mortgagor to cure his default on such mortgage.

As to your specific question, i.e., whether section 207(k) of the National Housing Act, as amended, 12 U.S.C. § 1713(k) (1970) contains sufficient legal authority to permit HUD to advance moneys from its appropriate Insurance Fund for the purpose of making repairs to multifamily projects after the insured mortgage on a project has gone into default and has been subsequently assigned to the Secretary of HUD, that section provides as follows:

> "The Secretary is authorized either to (1) acquire possession of and title to any property, covered by a mortgage insured under this section and assigned to him, by voluntary conveyance in extinguishment of the mortgage indebtedness, or (2) institute proceedings for foreclosure on the property covered by any such insured mortgage and prosecute such proceedings to conclusion. The Secretary at any sale under foreclosure may, in his discretion, for the protection of the General Insurance Fund, bid any sum up to but not in excess of the total unpaid indebtedness secured by the mortgage, plus taxes, insurance, foreclosure costs, fees, and other expenses, and may become the purchaser of the property at such sale. The Secretary is authorized to pay from the General Insurance Fund such sums as may be necessary to defray such taxes, insurance, costs, fees, and other expenses in connection with the acquisition or foreclosure of property under this section. Pending such acquisition by voluntary conveyance or by foreclosure, the Secretary is authorized, with respect to any mortgage assigned to him under the provisions of subsection (g) of this section, to exercise all the rights of a mortgagee under such mortgage, including the right to sell such mortgage, and to take such action and advance such sums as may be necessary to preserve or protect the lien of such mortgage."

Directing our attention to the final sentence of this provision, HUD's letter of March 12, 1975, makes the following argument concerning the proper interpretation of this provision:

> "A strict interpretation of the 'preserve or protect' clause would limit advances from the Insurance Funds to actions taken in an interim period during which HUD is preparing to acquire title by foreclosure or by a deed in lieu of foreclosure. The proposal to defer principal and interest does not contemplate that HUD anticipate the acquisition of title in the near future, but rather the purpose of the proposal is to enable the present mortgagor to continue to own and operate the project for the remaining term of the mortgage. Under this view, the word 'pending' has a limiting effect, restricting actions taken by the Secretary under this clause to those actions where acquisition of title is about to occur in the near future.
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> "A more liberal view of Section 207(k)--and the one we feel best comports with the underlying policy of the National Housing Act--would permit the Secretary to take all reasonably necessary steps to preserve or protect the lien on the mortgaged property. Since the money to finance these improvements will be advanced only after an analysis is made as to what repairs are necessary to prevent further deterioration of the project and to insure that the project complies with our minimum housing standards, the cost of the improvements should be considered as an expense necessary to preserve and protect our lien of the mortgage. The 'pending' clause should not be construed as a limitation on the Secretary's discretionary power to act. Rather, the word 'pending' should be interpreted to mean 'until', and should not be considered as constraining the Secretary to act only where he intends to acquire title within a short period of time. In other words, where the Secretary is the mortgagee, he may use whatever reasonable steps are necessary to preserve and protect the lien of the mortgage until title is acquired; once he has acquired title, the Secretary's rights are defined by Section 207(l)."

"We would like to further bring to your attention an observation with respect to the history of section 207(k). Prior to 1964 this section required the Secretary to foreclose a multifamily project within one year of default. This provision was deleted by the Housing Act of 1964. The legislative history for this deletion is sparse. The effect of the deletion, however, is consistent with the more liberal view of the meaning to be accorded the 'preserve or protect' clause, as it would seem to evidence Congressional intent that the Secretary must have broad discretionary power to determine when to foreclose and when to forbear. It is essential for the Secretary, in order to provide effective administration, to be able to assert the same rights as a private mortgagee when a mortgage is assigned to him, which includes the right to loan funds to make needed repairs."

The original language of the last quoted code provision required the Commissioner (of the Federal Housing Administration (FHA) to initiate foreclosure proceedings within one year after default unless the "defaulted" property had been voluntarily conveyed to HUD prior thereto. The specific language that established the one year period was set forth in the second sentence of the original provision and read as follows:

"* * * The Commissioner shall so acquire possession of and title to the property by voluntary conveyance or institute foreclosure proceedings as provided in this section within a period of one year from the date on which any such mortgage becomes in default under its terms or under the regulations prescribed by the Commissioner: Provided, That the foregoing provisions shall not be construed in any manner to limit the power of the Commissioner to foreclose on the mortgaged property after the expiration of such period, or the right of the mortgagor to reinstate the mortgage by the payment, prior to the expiration of such period, of all delinquencies thereunder."

However, section 108 of the Housing Act of 1964, approved September 2, 1964, Pub. L. No. 88-560, 78 Stat. 769, 776, amended 12 U.S.C. § 1713(k) by deleting this sentence from the provision. An examination of the following Congressional explanation for such deletion is relevant to our consideration:

"ELIMINATION OF MANDATORY ACQUISITION OR FORECLOSURE WITHIN 1 YEAR OF MULTIFAMILY PROJECT IN DEFAULT

"Section 505 of the bill would eliminate the requirement in existing law that FHA acquire title to the project or commence foreclosure of of an assigned mortgage within 1 year from the date of default in a mortgage insured by the FHA covering a multifamily housing project.

"Elimination of this requirement would make it possible, in some instances, to work out arrangements with mortgagors under which a defaulted mortgage could eventually be reinstated. The deletion of the 1-year requirement would give FHA latitude to consider each case on its own merits and to take such action as is required in each case.

"For example, situations arise where the economic conditions of a locality decline and as a result of the decline vacancies occur in rental housing. Often the mortgagors of multifamily projects find that they can no longer meet their amortization payments, and the mortgages go into default. One year from the date of default, the FHA must acquire title to the project, or commence foreclosure action, regardless of the fact that at the end of that year the economic conditions of the area may be improving and within 2 or 3 months hence rental accommodations may be in large demand. Under existing law the Commissioner has no flexibility in situations of this type.

"Acquisition of a multifamily housing project by foreclosure is, at best, a drawn-out and costly procedure. The foreclosure process has many weaknesses. Projects are usually operated by court-appointed receivers who cannot be expected to have as much interest in the project as the mortgagor. Once a project is acquired by FHA, contracts are let to managing agents who also do not have the same interest as the mortgagor. The FHA often goes to considerable expense to fix up a project and then sells it at a price less than the outstanding balance of the mortgage. The purchasers are frequently

speculators with no long-range interest in developing soundly operated projects. Foreclosure should therefore be avoided whenever possible and where the mortgagor can be expected within a reasonable amount of time to achieve project income that will permit curing the default.

"The committee believes that this amendment is in keeping with the new authority which would be vested in the FHA Commissioner by section 101 of the bill, supra, which deals with forebearance for home mortgagors.

"The committee has been advised that if the 1-year requirement is eliminated, the FHA would not hold foreclosure action or action to acquire title in abeyance indefinitely, but where there is no hope of reinstatement or the project is being mismanaged, foreclosure would be undertaken as soon as possible after a default. In this connection the committee wishes to explain that the primary purpose of the amendment is to give the FHA the discretion to work with a mortgagor, in a promising case only, for a reinstatement of the loan." (Emphasis added.) See S. Rep. No. 1265, 88th Cong. 2d Sess., 39, 40 (1964).

The above-quoted legislative history discloses that the purpose of the 1964 amendment was to give HUD some flexibility to consider each default case on its merits and to enable it in some instances to work out arrangements with mortgagors under which the defaulted mortgages could be reinstated, rather than to have HUD acquire title at the end of the one year default period, without regard to whether the mortgagor might be able to cure the default within a reasonable time after the expiration of the one year period. The legislative history makes it clear that foreclosure should be avoided whenever possible. However, the legislative history also makes clear that foreclosure should be waived only where the mortgagor "can be expected within a reasonable amount of time to achieve project income that will permit curing the default" (emphasis added), and that FHA "would not hold foreclosure action or action to acquire title in abeyance indefinitely." In this connection note the statement in the quoted legislative history to the effect that the amendment contemplated the Secretary not acquiring title or foreclosing on the property where it appeared that at the end of the first year from date of default, economic conditions might be improving and that within "2 or 3 months hence rental

accommodations may be in large demand." Thus, it would appear from the tenor of the legislative history that the 1964 amendment to the section in question contemplated that the Secretary would not forbear acquiring title if the default would not be, or was not, cured within a reasonable period of time after the expiration of a one year period.

Taking the foregoing into consideration, it is our view that the language of section 207(k) will legally permit the Secretary of HUD to advance money from the appropriate Insurance Fund to make necessary repairs to property covered by mortgages assigned to him upon default, until (1) the default is cured (either by the mortgage being brought current or by it being recast to defer a portion of the monthly principal and interest payments to the end of the mortgage term) or (2) title to the property is acquired by HUD, provided that the default is cured or title is acquired by the Secretary within a reasonable period of time after the expiration of one year from the date of the default. What constitutes a reasonable period of time would depend on the facts and circumstances in each case. Further, once the default is cured and the loan reinstated there would be no basis for the Secretary using the Insurance Fund to keep the property in repair.

The question presented is answered accordingly.

R.F.KELLER

(Deputy) Comptroller General
of the United States